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No. 00-637

In The

# Supreme Court of the United States

JOSEPH AND ELIZABETH BARTON-DOBENIN,

*Petitioners,*

v.

KANSAS DEPARTMENT OF REVENUE,

*Respondent.*

**On Petition For Writ Of Certiorari To The Kansas Supreme Court**

## RESPONDENT'S BRIEF IN OPPOSITION

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16 pp

## TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ..... ii

STATEMENT OF THE CASE ..... 1

REASONS WHY THE PETITION SHOULD BE DENIED ..... 2

I. The Decision Below Does Not Conflict With Any Decisions By Courts In Other States ..... 2

II. The Decision Below Does Not Conflict With Any Of This Court's Decisions ..... 4

III. Petitioner's Remaining Contentions Are Without Merit ..... 10

CONCLUSION ..... 12

## TABLE OF AUTHORITIES

Page

CASES

*Camps Newfound/Owatonna v. Town of Harrison, Maine*, 520 U.S. 564 (1997) ..... 8

*Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977) ..... 5

*Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159 (1983) ..... 7, 8, 10

*Fulton Corp. v. Faulkner*, 516 U.S. 325 (1996) ..... 7

*General Motors Corp. v. Tracy*, 519 U.S. 278 (1997) ..... 5

*Goldberg v. Sweet*, 488 U.S. 252 (1989) ..... 5

*Guzzardi v. Director, Division of Taxation*, 15 N.J. Tax 395 (1995) ..... 3

*Itel Containers International Corp. v. Huddleston*, 507 U.S. 60 (1993) ..... 9

*Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979) ..... 5, 9

*Keller v. Dept. of Revenue*, 872 P.2d 414 (Or. 1994) ..... 3

*Kraft, Inc. v. Iowa Dept. of Revenue*, 505 U.S. 71 (1992) ..... 8, 9

*Ludka v. Dept. of Treasury*, 399 N.W.2d 490 (Mich. App. 1986) ..... 3

*Luther v. Commissioner of Revenue*, 588 N.W.2d 502 (Minn. 1999), *cert. denied* ___ U.S. ___, 145 L.Ed.2d 57, 120 S.Ct. 66 (1999) ..... 2, 3, 4, 5

*Tamagni v. Tax Appeals Tribunal*, 695 N.E.2d 1125 (N.Y. 1998), *cert. denied* ___ U.S. ___, 142 L.Ed.2d 280, 119 S.Ct. 340 (1998) ..... 3, 4, 5

TABLE OF AUTHORITIES – Continued

Page

*United States v. Lopez*, 514 U.S. 549 (1995) .....5, 6

*Wardair Canada v. Florida Dept. of Revenue*, 477 U.S. 1 (1986) ..... 9

*Zunamon v. Zehnder*, 719 N.E.2d 130 (Ill. App. 1 Dist. 1999), *cert. denied* ___ U.S. ___, 147 L.Ed.2d 963 (2000) .....3, 5

STATUTES

1997 Kan. Sess. Laws ch. 126, § 48..... 2

OTHER AUTHORITIES

Hellerstein & Hellerstein, *State Taxation*, Vol. II (3rd Ed.) ..... 12

## STATEMENT OF THE CASE

We supplement the facts stated in the Petition as follows. First, the national government of the Czech Republic imposed the foreign income taxes paid by Petitioner and he received a federal income tax credit for those tax payments from the national government of the United States. (Petition, Appendix A at 4a). Petitioner did not pay any taxes to a sub-national government of the Czech Republic. (Record, Vol. V at 27).

Second, during the tax year at issue there was in force an income tax treaty between the Czech Republic and the United States designed to reduce or eliminate double taxation of income earned by residents of either country from sources within the other and to prevent avoidance and evasion of the income taxes of the two countries. (Record, Vol. IV at 13). The treaty provides relief from double taxation by requiring the country of residence to grant a credit for taxes paid to the country of source. (*Id.* at 14). With regard to the United States, the treaty's relief provision applies to income taxes imposed by the Internal Revenue Code but not to income taxes imposed by sub-national units of government such as the State of Kansas. (*Id.* at 26).

Finally, the Kansas Department of Revenue determined that Petitioner owed $113,074 in Kansas income tax during the year in question. (Petition at 4). The parties have stipulated that had Petitioner's income-producing properties been located in Missouri instead of the Czech Republic, his total State income tax liability (Kansas and Missouri) would have also been $113,074. (Petition, Appendix C at 32a-34a).

## REASONS WHY THE PETITION SHOULD BE DENIED

### I. The Decision Below Does Not Conflict With Any Decisions By Courts In Other States.

Petitioner challenges a Kansas statute that was amended in 1997 to do away with the practice of allowing resident individuals a credit for income taxes paid to other States but not to foreign countries. 1997 Kan. Sess. Laws ch. 126, § 48. In light of the amendment, the alleged constitutional infirmity of the Kansas tax system has already been addressed.

Courts are uniform in their view that a State's decision not to allow its residents a credit for taxes paid to other jurisdictions does not raise Commerce Clause concerns. The Court has consistently declined to review those decisions and this case should be treated no differently, particularly since Kansas is not a State in which this controversy is "live" and ongoing.

*Luther v. Commissioner of Revenue*, 588 N.W.2d 502 (Minn. 1999), *cert. denied* ___ U.S. ___, 145 L.Ed.2d 57, 120 S.Ct. 66 (1999), rejected the taxpayer's contention that her inability to claim a credit for taxes paid to Florida violated the Commerce Clause. Relying on many of the same authorities cited by the Kansas Supreme Court below, *Luther* concluded that the tax was based upon the taxpayer's substantial contacts with Minnesota and the services, benefits and protections provided to her and did not implicate the Commerce Clause. 588 N.W.2d at 511-12.

*Tamagni v. Tax Appeals Tribunal*, 695 N.E.2d 1125 (N.Y. 1998), *cert. denied* ___ U.S. ___, 142 L.Ed.2d 280, 119 S.Ct. 340 (1998), rejected a challenge to New York's failure to allow a credit for taxes paid to New Jersey. *Tamagni* held that the tax was based on the taxpayer's resident status and his maintenance of an abode within the State without regard to any economic activity incidental to his presence there. 695 N.E.2d at 1130. Consequently, the tax did not implicate the Commerce Clause.[1]

It is noteworthy that Petitioner's connections with Kansas are much stronger than those between the taxpayers and the taxing States in the above-mentioned cases. The taxpayer in *Luther* was domiciled in Florida but was deemed to be a "nondomiciliary resident" of Minnesota based on her ownership of a summer home and her substantial presence within the State. Likewise, the taxpayer in *Tamagni* resided in New Jersey but was considered a "statutory resident" of New York based on his ownership of an apartment in New York City and his

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[1] *See also Zunamon v. Zehnder*, 719 N.E.2d 130 (Ill. App. 1 Dist. 1999), *cert. denied* ___ U.S. ___, 147 L.Ed.2d 963 (2000) (denial of credit claimed by resident trusts for taxes paid to other states did not violate the Commerce Clause). Other state court decisions of note are *Ludka v. Dept. of Treasury*, 399 N.W.2d 490 (Mich. App. 1986) (upheld denial of credit claimed by resident taxpayer for income taxes paid to Belgium); *Keller v. Dept. of Revenue*, 872 P.2d 414 (Or. 1994) (Oregon's failure to allow resident a credit for Business and Occupation Tax paid to state of Washington did not discriminate against interstate commerce); *Guzzardi v. Director, Division of Taxation*, 15 N.J. Tax 395 (1995) (upheld denial of credit claimed by New Jersey resident for taxes paid to Pennsylvania; Commerce Clause held not to apply).

frequent presence in New York in connection with business matters.

Here, Petitioner has resided in Kansas since 1958, he was employed for many years by the State of Kansas and he files his income tax returns as a Kansas resident. (Petition, Appendix C at 29a, 31a). Since the taxpayers' activities in *Luther* and *Tamagni* did not implicate the Commerce Clause it must surely be the case that Petitioner's connections with foreign commerce, which are even more attenuated, do not either.[2] Further, since the Court has declined to review those cases, it would presumably have no interest in reviewing this one.

## II. The Decision Below Does Not Conflict With Any Of This Court's Decisions.

The decision below does not conflict with any of this Court's decisions. Historically, the Court has been reluctant to interfere with a State's taxation of its own residents,[3] a process in which revenue is raised from those who benefit most directly from the services provided by

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[2] As the court below stated, Petitioner's claim to foreign commerce is "much more tenuous" than that in other cases in which the Foreign Commerce Clause has been invoked. (Petition, Appendix A at 15a).

[3] *See* Petition, Appendix A at 11a ("Much has been written and numerous cases have been decided by the United States Supreme Court regarding the States' power to regulate matters affecting commerce. . . . However, very little guidance is given by the Court upon the application of the dormant Foreign Commerce Clause to the activity we now consider.")

the State. Further, Petitioner's contentions are inconsistent with established Commerce Clause jurisprudence and with the limitations inherent in the Commerce Clause itself.

The purpose of the Commerce Clause is to protect markets and participants in markets, not taxpayers as such. *General Motors Corp. v. Tracy*, 519 U.S. 278, 300 (1997). It is not designed to protect individuals from their own State taxes. *Goldberg v. Sweet*, 488 U.S. 252, 266 (1989). These decisions were relied upon in the opinion below (Petition, Appendix A at 14a), and also in *Luther*, 588 N.W.2d at 511, *Tamagni*, 695 N.W.2d at 1131, 1134, and *Zunamon*, 719 N.E.2d at 137. Further, they demonstrate that Petitioner's claim – which is premised on the theory that he as an individual citizen is being denied constitutional protection (Petition at 17) – is fundamentally flawed.

Petitioner ignores several of this Court's decisions that bear directly upon the issues in this case. First, he fails to explain how this case could be decided within the context of the Court's established Commerce Clause jurisprudence. The Petition contains only a fleeting reference to *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977) (Petition at 8 n.2), and makes no mention of *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979), despite the fact that these cases set forth the analytical framework used to determine the validity of a state tax challenged under the Interstate (*Complete Auto*) and Foreign (*Japan Line*) prongs of the Commerce Clause.

Second, Petitioner fails to discuss *United States v. Lopez*, 514 U.S. 549 (1995), which was central to the lower

court's determination that the tax in question does not implicate the Commerce Clause. (Petition, Appendix A at 10a, 14a, 18a). *Lopez* rejected the contention that the Federal Government's regulatory authority extends to areas in which States historically have been sovereign. 514 U.S. 564. In this regard, a state's right to levy a tax on its own residents must surely be among the most fundamental attributes of sovereignty.

Moreover, Petitioner's contention that the lower court carved out an exception to the Commerce Clause (Petition at 8), is inaccurate. Instead, the court sought to determine whether, as a threshold matter, the tax affects activities having a "substantial relation" to commerce. (Petition, Appendix A at 18a).[4] Because it found that the Commerce Clause was not implicated, the lower court never reached the question of whether the Kansas tax system discriminates against foreign commerce. (Petition at 7). In fact, at no stage in these proceedings has any court or administrative tribunal addressed the merits of Petitioner's discrimination claim. Consequently, if this Court were to grant the Petition it would be called upon to decide this issue in the first instance rather than acting in its traditional role as a court of review.

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[4] As indicated by Petitioner's own statements, the impact of the Kansas tax on foreign commerce is insubstantial at best. *See* Petition at 18 ("the ability of the State of Kansas to tax, *even obliquely*, the petitioner's Czech business translates into *the potential* to directly discriminate against it . . . [l]eft unchecked, *the possibility remains* for even more egregious measures against foreign businesses") (emphasis added).

Third, *Container Corp. v. Franchise Tax Bd.*, 463 U.S. 159 (1983), which Petitioner also fails to mention, indicates that a State's decision not to allow a credit for taxes paid to foreign countries does not violate the Foreign Commerce Clause, particularly when a federal credit is available. As noted above, Petitioner has already received a federal income tax credit for the Czech tax on his foreign-source income.

*Container* states:

> And the grant of a credit, which is the approach taken by federal law, does not in fact entirely eliminate effective double taxation; the same income is still taxed twice, although the credit insures that the total tax is no greater than that which would be paid under the higher of the two tax rates involved. Moreover, *once the Federal Government has allowed a credit for foreign taxes on a particular intercorporate dividend, we are not persuaded why, as a logical matter, a State would have to grant another credit of its own,* since the federal credit would have already vindicated the goal of not subjecting the taxpayer to a higher tax burden than it would have to bear if its subsidiary's income were not taxed abroad.

463 U.S. at 191 n.30 (emphasis added).

By comparison, the cases that Petitioner does cite have little relevance in this context. *Fulton Corp. v. Faulkner*, 516 U.S. 325 (1996), was a case in which the discriminatory nature of the tax was unchallenged; the dispute centered on whether it could survive scrutiny as a "compensatory tax" designed to make interstate commerce bear a burden already borne by intrastate commerce. 516 U.S. at 331. This is not such a case. As mentioned above,

the allegedly discriminatory nature of the Kansas statute has yet to be considered, let alone established. Hence, whether it is a compensatory tax is hardly the issue.

*Camps Newfound/Owatonna v. Town of Harrison, Maine*, 520 U.S. 564 (1997), invalidated a local property tax that had the effect of discouraging interstate travel and favoring those who were not engaged in interstate commerce. The Court, however, has drawn a distinction between income taxes and ad valorem property taxes for purposes of its Foreign Commerce Clause analysis. *Container*, 463 U.S. at 188. Further, the Kansas tax is not imposed on persons or things in commerce (Petition, Appendix A at 11a), nor is there any claim that it favors in-state residents. Consequently, an inquiry different than that utilized in *Camps Newfound* is mandated in this instance.

Finally, *Kraft, Inc. v. Iowa Dept. of Revenue*, 505 U.S. 71 (1992), is but one in a legion of cases in which the Court has considered the validity of taxes imposed on corporations engaged in interstate and/or foreign commerce. Those decisions, however, have never been extended, either expressly or by implication, to the taxation of resident individuals. This distinction was vital for purposes of the decision below:

> While it is clear that a state income tax may, and in *Kraft* did, run afoul of the Foreign Commerce Clause, we think it significant that the credit given in this case and the state law concerned applies to a resident of the state of Kansas.

Petition, Appendix A at 13a.

Moreover, the Court's focus in *Kraft* was on the possibility that discriminatory treatment of foreign commerce

could create problems, such as the potential for international retaliation, that concern the Nation as a whole. 505 U.S. at 79, citing *Japan Line*, 441 U.S. at 450. But there can be no similar contention in this case. Any concerns on the part of the Czech Republic regarding double taxation were addressed in its treaty negotiations with the United States. Significantly, the treaty does not impose restrictions on the taxation of Czech-source income by subnational governments such as the State of Kansas.

When a State tax does not conflict with federal objectives expressed in international agreements, statutes and regulations, the Court has stated that the most rational inference to be drawn is that the tax is permitted. *Itel Containers International Corp. v. Huddleston*, 507 U.S. 60, 75 (1993).[5] This case compels a similar conclusion. Congress has spoken with regard to the taxation of income derived by U.S. citizens from sources in the Czech Republic and the Kansas tax is not inconsistent with the limitations Congress has seen fit to impose.

Similarly, the Court has stated that the Foreign Commerce Clause cannot be interpreted to demand that a State refrain from taxing any business transaction that is also potentially subject to taxation by a foreign sovereign. *Itel Containers*, 507 U.S. at 74. Such forbearance has been characterized as "extreme" and "one-sided." *Id.*, citing

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[5] *See also Wardair Canada v. Florida Dept. of Revenue*, 477 U.S. 1, 11-12 (1986) (where various international agreements entered into by the Federal Government prevented national governments, but not states or other political subdivisions, from taxing aviation fuel, the United States was deemed, by negative implication, to have acquiesced to the tax at issue).

*Container*, 463 U.S. at 193. Just as Kansas and other States have the right to tax their residents, the United States as a whole has a "sovereign right" to let the States tax as they please. *Container*, 463 U.S. at 194. Since there is no violation of international law in this instance, the Commerce Clause should not be construed to defeat the legitimate interests of the States and, arguably, the Federal Government.

## III. Petitioner's Remaining Contentions Are Without Merit.

Petitioner's eagerness to pique the Court's interest causes his remaining contentions to be contradictory and self-defeating. For example, he attempts to portray this case as being representative of the "new" technology-driven economy in which "pass-through" entities such as S Corporations, LLCs and LLPs use modern technology to compete in the global marketplace. (Petition at 9-10). This case, however, is hardly on the cutting edge. Petitioner is merely a private property owner who collects rent from his tenants. (Record, Vol. V at 26). To the extent the Court wishes to consider the application of the Commerce Clause to emerging trends in international business, this is not the case in which to do so. In reality, Petitioner's claim is simply that the lower court misapplied settled law, as evidenced by his contentions that the decision below was based on "formalisms" (Petition at 8), and "archaic notion[s]." (Petition at 21).

Petitioner attempts to equate the Kansas tax with an excise tax on residents for the privilege of doing business

in foreign countries (Petition at 19), which it most assuredly is not. The lower court found that the tax is not imposed on Petitioner's movement in foreign commerce nor is it a tax on his business for the services it provides. (Petition, Appendix A at 16a). Rather, it is "a personal income tax imposed on a resident of the state of Kansas for the purpose of reimbursing the state for the protections it affords the individual." (*Id.* at 19a). Plainly, while the Commerce Clause is admittedly broad in its scope, this case is on its utmost outer fringe.

Ultimately, Petitioner's claims fail due to his inability to come to grips with two overriding imperatives, the first of which is the unique relationship between a State and its residents. While Petitioner sees no difference between a tax on individuals and a tax on corporations, it is fundamental that citizens of the United States stand in a special relation to the States in which they reside and depend upon them for the most basic human services and protections. In contrast, corporations are creatures of statute and their *raison d'etre* is to engage in commercial activities. When viewed in this light it is unsurprising that the Court has never extended its Commerce Clause rulings involving the taxation of multi-state and multinational corporations to resident individuals. Petitioner does not explain why this case justifies a departure from that longstanding practice.

Second, as a practical matter, there can be no contention that domestic commerce is being favored over foreign commerce in this instance. Petitioner's Kansas income tax liability of $113,074 is precisely the same as the total amount of State income taxes that would be owed by a Kansas resident with the same amount of

income from sources in another State. To minimize duplicative taxation, States allow credits for income taxes paid by their residents to other States.[6] This system works well in most cases and is a reasonable way in which to balance the competing interests of States that have a right to tax the same income. To invalidate the Kansas statute and others like it because they do not allow a credit for taxes paid to foreign countries would result in widespread disruption with little or no corresponding benefit to the interests the Foreign Commerce Clause is designed to protect.

## CONCLUSION

For the foregoing reasons, the Petition for writ of certiorari to the Kansas Supreme Court should be denied.

Respectfully submitted,

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[6] *See* Hellerstein & Hellerstein, *State Taxation*, Vol. II (3rd Ed.) ¶20.10 ("every state with a broad-based personal income tax provides a credit for taxes that their residents pay to other states").